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June 27, 2003

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JUN 27 2003

FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

VIA HAND DELIVERY

Ms. Marlene H. Dortch
Secretary
Federal Communications Commission
445 12th Street, S.W.
Washington, D.C. 20554

Re: Notification of Oral and Written *Ex Parte* Communications
MB Docket No. 02-144 – Revisions to Cable Television Rate Regulations

Dear Ms. Dortch:

On June 26, 2003, Gary R. Matz, Vice President and Assistant General Counsel, Time Warner Cable, and Steven N. Teplitz, Vice President and Associate General Counsel of AOL Time Warner Inc., the parent company of Time Warner Cable, accompanied by Seth A. Davidson and Arthur H. Harding of Fleischman and Walsh, L.L.P., met with the following members of the Media Bureau staff to discuss the above-referenced proceeding: William Johnson, Peggy Greene, Mary Beth Murphy, John Norton, Steven Broeckaert, Kenneth Lewis, and Katie Costello.

The presentation made on behalf of Time Warner Cable during the meeting focused on (i) the need for continued Commission oversight of the local rate regulation process; (ii) clarification of the Commission's rules regarding the recovery of external costs associated with the carriage of locally originated channels; (iii) clarification of the Commission's rules regarding the establishment of rates for digital converters provided to basic-only customers; and (iv) proposals for streamlining the process of determining the presence of "effective competition." Included with this letter is a written outline of the points made on behalf of Time Warner Cable on each of these subjects. Pursuant to Section 1.1206(b) of the Commission's rules, an original and one copy of this letter and the attachments thereto are being submitted to the Secretary's

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office for inclusion in the record of the above-referenced proceeding and a copy is being provided to each of the participants in the meeting.

If there are any questions regarding this matter, please communicate directly with the undersigned.

Respectfully submitted,

Seth A. Davidson

cc: W. Johnson
P. Greene
M. Murphy
J. Norton
S. Broeckaert
K. Lewis
K. Costello

FCC REVIEW OF LOCAL RATE ORDERS

- **The FCC Should Not Give Increased Deference To Local Rate Orders.**
  - Congress sought to ensure national uniformity with respect to basic rate regulation.
    - √ Congress directed the FCC to establish rules and formulas to be applied by local governments in regulating basic rates as well as the guidelines and procedures concerning the implementation and enforcement of those rules and formulas.
    - √ Congress required local governments engaging in basic rate regulation to certify to the FCC that they will follow the federally-established rules and formulas.
    - √ Congress authorized the FCC to review basic rate decisions and take "appropriate" action where the local franchising authority has acted inconsistently with the federally-established rules.
  - Giving greater deference to local rate orders will produce a patchwork quilt of regulatory standards.
    - √ This lack of uniformity will greatly add to the cost and complexity of determining maximum permitted rates, as MSOs will have to tailor their rate calculations on a community-by-community basis to reflect varying local interpretations of the FCC's rules and forms.
  - Varying local interpretations of the FCC's rules also will impede the accomplishment of the national policy objectives underlying certain aspects of rate regulation, such as the calculation of equipment rates on an aggregated basis.

- **FCC Oversight of Local Rate Orders Remains Necessary.**
  - Local franchising authorities increasingly are imposing unnecessary and burdensome information requests on cable operators and then rejecting proposed rate adjustments on the grounds that the operator has failed to meet its burden of proof.
    - √ For example, some LFAs take the position that the signed "certification" of accuracy at the end of each form must be supplemented by sworn testimony from company officials with personal knowledge of all of the data underlying the entries on the form – an extremely burdensome demand where the operator computes its rates on a company-wide basis.
    - √ The FCC previously has stated that franchising authority information requests should be narrowly tailored and should state the reason the information is needed. The FCC needs to reiterate this standard and make clear that local officials are limited to requesting the source information (such as general ledger data) used by the operator in completing the rate form under review.

- The Commission should impose appropriate sanctions, including decertification and the assessment of attorney's fees, against local franchising authorities that flagrantly disregard the rules and reject proposed rate justifications on grounds extrinsic to the rate calculations.

  √ Congress clearly authorized the FCC to revoke the certification of local regulators who refuse to fulfill their obligation to follow the rules established by the Commission.

  √ When a local government flagrantly and frivolously ignores a cable operator's rate justification, it imposes unnecessary costs on the FCC, the operator, and ultimately, on consumers.

  √ While the FCC has been reluctant to impose sanctions on rogue local regulators, the current regulatory scheme has been in place for 10 years and the time has come for the FCC to take steps to deter regulatory abuses.

LOCAL ORIGINATION CHANNEL COST PASS THROUGH

- **The FCC Should Clarify The Rules Governing the External Cost Pass Through of Affiliated Local Origination Channels.**

  - The FCC has consistently encouraged cable operators to offer local origination programming, particularly local news and information programming. Indeed, at the recent NCTA convention, Chairman Powell made a point of congratulating cable operators that have launched local news channels. However, efforts to launch such channels are threatened by uncertainty and ambiguity regarding the rules governing the external cost pass through of the cost of such channels.

    √ Locally originated channels typically are not widely distributed by unaffiliated operators and thus have no "prevailing market price." Section 76.922(f) provides that where there is no prevailing market price for affiliated programming, the cost pass through for such programming should reflect "fair market value."

    √ However, Section 76.924(i)(1) provides that the cost of transactions involving affiliated assets should be the lower of their "cost to the originating activity of the affiliated group less all applicable valuation reserves, or their fair market value."

    √ And Section 76.924(i)(3) provides that the transactions involving affiliated services should be valued "at cost."

  - A pass through standard that allows local government officials to make subjective determinations regarding the "fair market value" of a locally originated channel will create uncertainty and deter the creation of such channels. Moreover, a standard that permits local governments to engage in an intrusive assessment of the "reasonableness" of the specific costs incurred in providing such a channel poses a substantial threat to first amendment values.

    √ For example, local governments should not be permitted to judge whether the compensation paid to the anchor of local news channel is "excessive."

  - The FCC should clarify that, in the case of a locally-originated channel that is not widely distributed to unaffiliated cable operators, cable operators may establish the cost of the channel by means of an abbreviated cost-of-service calculation based on general ledger information. The role of the local franchising authority in reviewing this cost calculation should be limited to assessing its completeness and mathematical accuracy.

    √ If the amount that the operator elects to pass through is equal to or less than the cost of providing the channel, that amount should be deemed to reflect the "fair market value" of the channel.

EQUIPMENT AGGREGATION RULES

- **The FCC's Equipment Aggregation Rules Assume That Equipment Used By Basic – Only Subscribers Is Less Expensive Than Equipment Used By Other Customers.**

  - Section 623(a)(7) of the Communications Act, which generally permits cable operators to establish maximum permitted equipment rates on an aggregated basis, bars such aggregation with respect to equipment used by subscribers who receive only a rate regulated basic tier.

  - The FCC has found that the provision relating to basic-only equipment was intended to ensure that basic-only subscribers do not bear the costs of more sophisticated equipment used by non basic only subscribers. Assuming that that equipment used by basic-only customers is less sophisticated – and less expensive – than equipment used by other subscribers, the FCC ruled that the limitation on aggregation applies to subscribers, not to a particular type of equipment.

- **The FCC Should Clarify The Application Of the Equipment Aggregations Rules To Digital Set-Tops Leased By Basic-Only Customers.**

  - As the digital transition progresses, operators increasingly will be transmitting broadcast stations in digital format. For the foreseeable future, most subscribers will need an additional set-top device in order to receive a cable operator's digital transmissions.

  - Section 623 requires rate regulated cable operators to offer digitally transmitted broadcast signals as part of the basic tier. Thus, basic-only customers who want to receive the full complement of basic tier channels will need the same digital box as other customers. However, the FCC also has ruled that basic-only customers can elect not to lease a digital box even though it means that they won't receive all of the basic channels.

  - Because basic-only subscribers have the option of electing not to receive digital basic channels, cable operators should be permitted to charge the same rate for leasing a digital box to a basic-only customer as is charged to a non-basic only customer.

    √ Indeed, aggregating digital boxes with other basic-only equipment will produce higher equipment prices for basic-only customers who do not elect to receive (or who subscribe to systems that do not offer) digital basic tier channels – exactly the result that Congress sought to avoid.

EFFECTIVE COMPETITION

- **Streamlining Effective Competition Determinations Benefits All Interested Parties.**
  - It will ease administrative burdens on cable operators, local franchising authorities and the FCC staff.
  - It will reduce the number of contested proceedings
  - It will promote timely, efficient and consistent action by Commission.
- **Adjusting the Burden Of Proof**
  - Assigning the burden of proof was a close call even back in 1994 and the dramatic change in the competitive landscape since then warrants revisiting the presumption that effective competition does not exist.
  - Effective competition should be presumed to exist throughout any state with DBS penetration above a specified threshold, e.g., 20%.
    - √ LFAs could rebut the presumption with community-specific showings.
    - √ FCC would need to require SkyTRENDS or DBS providers to make penetration data available to LFAs.
    - √ LFAs seeking to regulate rates for the first time would have to show the absence of effective competition, much as they are required to do when re-certifying after a finding of effective competition.
  - At a very minimum, the burden of proof should be neutral.
    - √ With no presumption that a particular community either is or is not subject to effective competition, determinations would be based on a preponderance of the evidence.
    - √ Unopposed petitions could be granted automatically at close of comment period.
- **Simplifying DBS-Based Effective Competition Showings**
  - The Commission should take official notice that DirecTV and EchoStar satisfy the first prong of the 50/15 competing provider test.
    - √ The Commission has repeatedly recognized that DBS is technically available throughout the continental United States.
    - √ There are no regulatory, technical or other impediments to the receipt of DBS service.

- √ DirecTV and EchoStar unquestionably offer programming "comparable" (as defined by the FCC rules) to that of any cable operator.

- √ It is beyond dispute that U.S. consumers today are universally "reasonably aware" of the availability of DBS service.

- √ DirecTV, EchoStar and retailers that offer their products advertise and market extensively through national, regional and local media, including newspapers and magazines, television and radio, and the Internet, as well as by means of point-of-purchase brochures, door hangers, direct mail solicitations, and e-mail.

- √ According to its most recent 10-K filing with the Securities and Exchange Commission, EchoStar spent well over $100 million on advertising and related expenses a year, and had overall marketing expenses exceeding $1 billion a year, for 2000 and 2001.

- √ According to VMS, a media tracking service, there have been over 200 national and local ads on broadcast and cable channels since January 2002 for DirecTV and EchoStar's Dish Network.

- √ The fact that DBS penetration in the United States now exceeds 20 percent justifies official notice by the Commission that potential subscribers are reasonably aware of this service.

- o Where DBS subscribership in a particular community exceeds 15%, consumers obviously are reasonably aware of the availability of DBS.

- o Effective competition showings could then properly focus solely on whether the 15% competitive penetration standard has been met.